

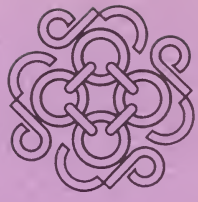
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Dairy Cooperatives



FARMER COOPERATIVES IN THE UNITED STATES
COOPERATIVE INFORMATION REPORT 1
SECTION 16

UNITED STATES DEPARTMENT OF AGRICULTURE
AGRICULTURAL COOPERATIVE SERVICE



Cover

Tillamook cheese, being made here in its Oregon plant, sells for a premium throughout Western U.S.

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Cooperative Information Report 1,

Section 16

November 1986

Two-hundred-pound drums of dehydrated cheese are ready for blending in a plant owned by Mid-America Dairymen, Inc., Springfield, MO.



Dairy Cooperatives



Number and Volume

The Nation's dairy cooperatives continue to follow the industry trend toward fewer but larger firms. By 1980 there were about 435 cooperatives, down from 592 in 1973, 1,250 in 1964, and 1,550 in 1957. Except for the 1964-73 period, numbers of dairy cooperatives have declined about 3 percent a year since 1957. A surge of mergers and consolidations during 1964-73 accelerated the decline rate for this period to 8 percent.

During fiscal year 1976-77,¹ about 190,000 farmers were members of dairy cooperatives, including farmers who belonged to more than one. About 105,000 farmer members shipped grade A milk to Federal order milk markets. Most of the remaining 85,000 members shipped non-grade A milk to manufacturing plants—primarily plants operated by their cooperatives. The remaining grade A milk went largely to State-regulated fluid milk markets and a small amount to nonregulated fluid milk markets.

Also during 1976-77, some 412,000 farm operations had milk cows; about 260,000 had five or more cows. Seventy-three percent of those farm operations with five or more milk cows belonged to dairy cooperatives. It was further estimated that the number of farms selling milk in 1980 had declined to about 215,000, and the number marketing milk through cooperatives was about 160,000, or 74 percent of the total.

In 1973, cooperatives marketed about 75 percent of the total milk sold to plants and dealers. They marketed 81 percent of the grade A milk and 55 percent of the non-grade A milk. At that time, 78 percent of the Nation's total milk sales to plants and dealers was grade A with the remaining 22 percent non-grade A.

¹Fiscal years for cooperatives ending during July 1, 1976 to July 1, 1977.

Since 1973, grade A milk sales for the Nation have increased to 85 percent of total, but by 1980 cooperatives' share of sales declined to 79 percent. While non-grade A milk sales declined nationally, cooperatives' share increased slightly to 57 percent in 1980. Thus, in 1980, cooperatives' share of total milk sold to plants and dealers rose slightly to 77 percent, representing a leveling of the longer term trend to an increased cooperative market share.

Cooperatives market their members' milk in many forms. In 1980, their raw milk sales, the largest category of product sales, was 52 percent of total milk receipts by all plants and dealers, a moderate increase from the 47 percent noted in 1973. Milk processed and manufactured by cooperatives increased significantly from 1973 to 1980, reaching 35 percent of all milk sold to plants and dealers in the Nation, up from 28 percent in the earlier year.

Cooperatives' share of major dairy products produced and distributed in 1980 was:

<i>Product</i>	<i>Percent of total</i>
Dry milk products	87
Butter	64
Natural cheese	47
Cottage cheese	33
Ice cream	20
Packaged fluid milk	16
Frozen product mix	6

Origin and Development

Dairy farmers pioneered the application of cooperative principles in marketing U.S. farm products. In 1810, farmers started a dairy cooperative in Goshen, CT and a cheese cooperative in South Trenton, NY. But widespread use of cooperatives developed much later with the advent of the factory system to make cheese and butter. Credit for establishing the first real cheese factory that served as a model and incentive for developing the cooperative system is generally given to Jesse Williams of Oneida County, NY. He was an experienced and skillful cheesemaker whose product brought premium prices. He proposed collecting milk daily from several neighboring farms to be made into cheese by a skilled operator. From this idea in 1851, sprang the association cheese factory system, butter factories, and other kinds of milk plants. By 1856, a cooperative butter creamery had been organized in Orange County, NY.



In early days of commercial dairying, farmers left milk cans on raised platforms beside the road. They were collected and hauled to plants like the one below operated by Golden Guernsey Dairy Cooperative, Milwaukee, WI.



Dairy Manufacturing Cooperatives

Milk's perishable nature and its year round production, its isolation from city markets, the cooperative tradition carried from home countries of North European immigrant dairy farmers, and the economies available from jointly owned milk manufacturing plants all combined to rapidly increase dairy cooperatives in the late 19th and early 20th centuries. Most of these were organized in the Northern States. Most of the thousands of small rural cheese factories and creameries (butter churning plants) organized in this period had some cooperative features, although many were not strictly cooperative by today's definitions. Many early factories in New York State included the following in their organizing plans:

1. Form a corporation under the general manufacturing law.
2. Distribute as much stock as possible in small shares among dairy-men in the local area to secure patronage and create a general desire for the association to succeed.
3. Give a board of trustees responsibility for managing the association.
4. Elect trustees at the annual stockholders' meeting.
5. Trustees elect board officers, form committees to oversee the business, and employ a person to direct factory operations.
6. Distribute all monies received for products sold less all costs including depreciation and interest on the investment to patrons according to the amount of milk delivered by each.²

Other factories developed where the proprietor or company bought the milk or cream from producers at prices mutually agreed upon from time to time and assumed all expenses, risk, and returns of the business. Profits were distributed only to stockholders on the basis of shares owned.

Cooperative Cheese Factories and Creameries

By 1870, use of cheese factories was expanding. From New York they spread first to Pennsylvania and Ohio then to other States, east and west. In 1900, almost 3,000 existed nationwide, including many small-volume factories. New York and Wisconsin had about 1,000 each. Possibly one-third were operated as cooperatives.

²Gardner, Chastina. Beginnings of Cooperative Dairy Organizations, USDA, BAE, Division of Cooperative Marketing. A preliminary report, June 1927.

Because dairy farms were relatively small and remotely located, the number of creameries grew slowly until mechanical cream separators were introduced about 1890. By 1900, there were some 6,000 creameries, more than twice the number of cheese factories. Again, cooperatives operated about one-third.

Cooperative creameries were generally organized in areas where, because of distance from city markets and small size of dairy farms, a large portion of the milk produced could best be marketed for butter production. While some cooperative creameries existed in most States, they were concentrated in the Midwestern States, particularly Minnesota, Iowa, and Wisconsin.

Most cooperative creameries and cheese factories began as local organizations handling relatively small volumes of milk and/or cream. The volume received by these plants were limited to the amount of milk or cream that could be assembled and delivered in horsedrawn wagons once or even twice a day.

These many thousands of small cooperative ventures varied widely in the extent to which they adopted and practiced what today are considered true cooperative principles. Many sold to both members and non-members, and some were partially financed with equity investments of nonproducers. These cooperatives flourished and waned through the late 19th and early 20th century with changes in economic conditions, dairy plant technology, and local farming practices. But they provided markets for the Nation's growing numbers of dairy farms, mostly located in isolated rural areas lacking today's modern road transportation network. Generally, these predecessors to our present day dairy cooperatives served as proving grounds where dairy farmers learned to organize and operate their own cooperative business enterprises.

Few data exist on the growth in number of cooperative creameries and cheese factories. By 1922, the total number had declined to 1,610. Introduction of motorized transportation led to cream assembly over wider areas, permitting the number of cooperative creameries to remain relatively constant until the late 1930's. The average lifespan for creameries before 1940 was almost 15 years. Increased food needs during World War II brought a dramatic shift from marketing cream to marketing whole milk, resulting in a rapid decline in number of creameries.

In 1957, the number of cooperative creameries had further declined to about 500 and by 1980 they had either all disappeared or shifted to raw whole milk receiving and shipping operations. Many of those that vanished had joined with others in forming large dairy manufacturing cooperatives.

Cheesemaking cooperatives declined in number similarly to the

cooperative creameries. The average life for cheesemaking cooperatives before 1940 was about 13.5 years. By 1980, there were 174 cheesemaking cooperatives.

Federated Sales Cooperatives

The 1920's witnessed organization and growth of large-scale dairy organizations, particularly noncooperative corporations. Earlier, cooperatives began expanding their volume and improving their marketing position using federated marketing organizations. In 1909, nine cooperatives in Tillamook County, OR, all using the same salesmen, organized the Tillamook County Creamery Association to improve their product quality and coordinate marketing and other matters of mutual interest. In 1911, a group of California cooperative creameries organized Challenge Cream and Butter Association as the sole agency for marketing their butter and other products. Later the association's membership was expanded to include cooperatives in a number of Western States. In 1921, a group of cooperative creameries in Minnesota formed Minnesota Cooperative Creamery Association to produce high-quality butter and sell it for member creameries. In 1926, its name was changed to Land O'Lakes, Inc. Other major federated sales cooperatives were soon established: Illinois Producers Creameries, Darigold in Washington (Seattle), State Brand Creameries in Iowa, Valley Lea Dairies in Indiana, and several in Wisconsin.

Other Milk Manufacturing Cooperatives

The condensed milk industry began at the same time as the factory system, but cooperatives did not play an important part. By the 1920's, however, some cooperatives had acquired milk evaporating facilities as an alternative to making butter or cheese. By the 1930's some creameries were installing milk drying facilities to provide a market for buttermilk and skim milk.

World War II brought an increased need for manufacturing dairy products, particularly dry milk products. Through lend-lease funds, the Federal Government financed the construction of several cooperative milk drying plants. Many farmers shifted from marketing farm-separated cream to whole milk. By 1944, some 200 cooperative plants were manufacturing nonfat dry milk.

Improvements in transportation, including tank assembly of milk, expanded the supply area for individual milk manufacturing plants and increased competition between plants for milk in the volume needed for low-cost operations. Increased mobility of milk not only accelerated the

trend toward large commercial dairy farms but also toward large-scale plant operations, improved plant technology, and declining numbers of plants and cooperatives.

By 1980, essentially all milk was assembled and transported from farms to plants in bulk. While grade A milk production reached 85 percent of total production in 1982, the amount used in fluid milk products continued to decline. This prompted greater milk manufacturing activities by cooperatives that had primarily shipped milk to fluid milk handlers. In some cases these cooperatives can now be classified as milk manufacturing cooperatives using more milk in manufacturing operations than they sell as raw milk.

Fluid Milk Marketing Cooperatives

Organized marketing of raw milk for fluid consumption began during the latter part of the 18th century in cities where families without cows were unable to obtain milk from a nearby producer. A system of middlemen between producers and consumers emerged from this historical pattern.

During the first half of the 19th century, before rail transportation and mechanical refrigeration, it became increasingly difficult for large cities to obtain adequate milk supplies from country dairy farms. To meet the demands for milk in large cities, distilleries often developed a milk production system within the city limits. Cows were generally housed in stables and fed distillery slop with a minimum amount of hay. The milk was of poor quality, partly because of abnormal feeding and otherwise poor care of cows in crowded, unsanitary stables, and partly because the milk was diluted with water at each sales level. Twice a day carriers delivered milk dipped from a can and poured into the customer's container.

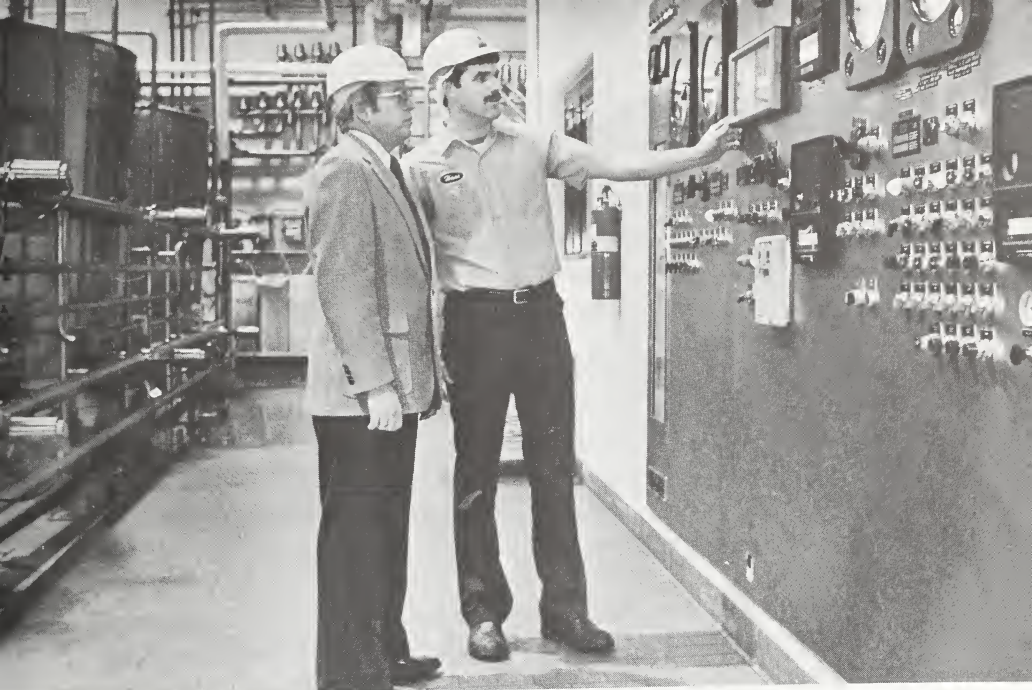
Development in Large City Markets

Cooperative development in marketing milk for fluid use before 1900 centered in the large cities in the eastern part of the United States and Chicago. As early as 1842, the Erie Railroad brought milk from Orange County, NY, to Jersey City, NJ, a distance of 80 miles. The Orange County Milk Association with 20 shares of stock owned mostly by local dairy farmers arranged these first shipments of "pure" country milk to a large city. This association began with some cooperative principles, but over time it became another company instead of a cooperative.



Modern technology of dairying is reflected in these facilities: Top—Springfield plant of Valley of Virginia Cooperative Milk Producers Association, Inc.; bottom—typical unloading of fluid milk transport trucks into a plant operated by Dairymen, Inc., Louisville, KY; . . .





...top—master control panel for Wisconsin Dairies, Inc., plant at Lancaster; bottom—cheddar cheese storage, Mid-America Dairymen, Inc., Springfield, MO.



Rapid construction of railroads in America during the middle and late 1800's permitted the increased supplies of "fresh country" milk to the cities, gradually replacing the inferior distillery milk. Cooperative development of bargaining by farmers with city milk dealers was sporadic. Rural isolation, the generally independent nature of most dairy farmers, and the formation of powerful milk dealers' organizations combined to suppress the growth of significant cooperatives.

Erratic and often chaotic pricing of milk for fluid uses and a growing practice by milk dealers of balancing their fluctuating supply needs by refusing to accept some producer's milk at times, finally led to the successful formation of large-scale cooperative bargaining organizations. The Dairymen's League Cooperative and the Chicago Milk Producers' Association, formed before 1910, were pioneer large-scale milk marketing associations that encouraged greater farmer control of milk pricing.

During the first half of the 20th century, those dairy cooperatives basically oriented to supplying milk for the fluid market gradually evolved into the three subclasses of cooperatives recognized today. These were the pure bargaining raw milk sales cooperatives, the bargaining-operating cooperatives, and the fluid milk processing cooperatives.

Pure Bargaining Raw Milk Sales Cooperatives

With the development of fluid milk markets came new and different milk marketing problems. Fluid milk buyers required higher quality milk than creameries and cheese factories, and the seasonal and daily supply-demand balance was more critical. Generally, farmers organized bargaining associations to provide the unity needed to obtain reasonable milk prices, market security, and better milk marketing conditions.

Pure bargaining associations are viewed today as a limited service type of raw milk sales cooperative. Originally they were organized by producers shipping milk to the major fluid milk markets, particularly in the Northeastern and North Central States. Many of the early organizations were short lived. They would operate for a time and then fold to be followed by another attempt. In 1925, some 40 bargaining associations made almost 25 percent of total dairy cooperative sales. In 1931, the number of associations had increased to 59 and sales volume to 40 percent. By 1980, 146 dairy cooperatives did not physically handle milk or dairy products—34 percent of all cooperatives. However, they accounted for only about 15 percent of milk sold to plants and dealers.

Several factors contributed to growth in number and size of bargain-

ing associations during the decade following World War I. Producers were dissatisfied because of the low milk prices before World War I and the rapidly declining demand following the war. Also, the legal status of cooperatives had been clarified already by several State and Federal statutes, including the Clayton Act in 1914 and the Capper-Volstead Act in 1922, exempting farmers forming cooperatives from some of the anti-trust laws.

Generally, bargaining associations incorporated and obtained a formal marketing agreement with their members. Activities of the association were financed by a small fee or an operating assessment of a few cents a hundredweight of milk marketed. Beginning with little capital and no facilities for handling milk, their bargaining strength depended largely on the support of all producers in the market. Operating assessments were set at a level that permitted earnings that were, in turn, largely retained to build equity capital.

Early bargaining associations quickly found increases in milk prices led to problems in disposing of surplus milk (milk not needed for fluid use). Thus, they pioneered pricing milk to dealers on a classified basis according to use and used audit procedures to assure proper payment by handlers. They also developed milk pooling systems including "base-excess" or "quota" plans for more equitable distribution of returns for different milk uses and seasonality of milk deliveries among members.

Continuing instability in fluid milk marketing during the 1930's led to State and Federal milk marketing orders incorporating milk pricing by classes according to its use and a number of other marketing principles pioneered by cooperatives. Implementation of the marketing orders generally required producer approval with cooperatives permitted to block vote their membership for or against the order. This, in turn, led to the organization of many new cooperatives, some formed as a first step in obtaining a milk marketing order and others formed to represent producer views different from those of the members of existing cooperatives.

Even though the long-term trend has been toward greater farmer membership in large-scale bargaining-operating cooperatives, a number of small pure bargaining cooperatives continue. Some survive by maintaining a close relationship with their milk buyers, permitting delivery of their full milk supply to the customer's plant. Others exist by obtaining needed services through affiliation with a large cooperative or through membership in a federated organization. Generally, these small cooperatives are not leaders in pricing or in improving overall marketing efficiency. They strive for market arrangements that permit them to gain most benefits developed by the larger bargaining cooperatives while avoiding some of the marketing costs.

Bargaining-Operating Cooperatives

Some raw milk sales cooperatives in the larger markets acquired milk manufacturing facilities as early as the 1920's to assure members a market for their milk. However, most of these cooperatives provided limited marketing services until the 1950's when the shift from can to bulk milk assembly triggered development of a new cooperative milk marketing system.

With the advent of milk assembly in bulk tanks and tank trucks, farm shipments greatly increased, partly because of the shift from daily to every-other-day farm pickups and partly because the surviving dairy farms were producing more milk. After terminating can-milk receiving operations, many handlers chose to specialize in fluid milk processing and distributing, and leave milk procurement and disposition of milk supplies not needed for fluid use to the cooperatives.

The larger cooperatives were the first to face the need for marketing adjustments. They had strengthened their marketing position and their members' market security by becoming major suppliers for one or more metropolitan markets. They soon had to deal with increased mobility of milk, both raw and packaged, and growing specialization by fluid milk buyers.

Recognizing that milk marketing was becoming regional, raw milk sales cooperatives in many areas began to unite in federated regional bargaining associations and pioneered regional pricing of milk in the 1960's. With a tightening of milk supplies in the late 1960's, they established over-order prices for Class I milk in Federal Milk Market Orders extending from the Great Lakes to the Gulf and Mexican border.

Bargaining through regional federations initially proved successful but difficulties developed. The mere logistics of obtaining approval of a pricing plan acceptable to member cooperatives was often burdensome and lengthy. Where disagreements developed, problems in obtaining member acceptance were greatly magnified. Also, disagreements could cause member cooperatives to withdraw and pursue an independent course.

A number of large regional and interregional federations have evolved and now play an important role in milk marketing. Their membership consists largely of regional bargaining-operating cooperatives. These regional federations perform a limited function of coordinating the activities of their member cooperatives in establishing a scale of regional and interregional service charges for milk above Federal order minimum levels. They also perform the valuable function of providing a



A major technological advance in milk handling occurred in the 1960s when on-farm sanitized bulk milk holding tanks, like this early model, replaced cans. Larger volumes of milk moved longer distances in refrigerated transports and "double-bottoms," such as the one below.



forum to adjust sales policies and coordinate raw milk shipments to buying handlers to lower trucking costs. Also, these federations unify and coordinate presentations made in Federal order hearings, which make adjustments in response to changes in market conditions. Examples of these large bargaining federations include the Regional Common Marketing Agency in New York and New England; Great Lakes Southern, operating from Michigan to Florida; and Central Milk Producers Cooperative in the Wisconsin-Chicago area.

By 1967, many dairy cooperatives began restructuring their organizations into large centralized bargaining-operating cooperatives supplying raw milk to fluid milk handlers over multimarket areas tailored to plant needs. They added or expanded milk manufacturing facilities as required to handle reserve milk supplies not needed for fluid use. By 1980, these cooperatives were not only providing fluid milk handlers with most of their milk, but were also producing a large proportion of the manufactured dairy products made by cooperatives. The operation of large manufacturing plants has evolved from a purely balancing "least-loss" function into important profit centers and now is a major function of most bargaining-operating cooperatives.

Fluid Milk Distributing Cooperatives

A relatively small number of fluid milk cooperatives have specialized in fluid milk packaging and distribution. Some were organized specifically to package and distribute milk. For example, health regulations requiring milk to be pasteurized encouraged producer distributors in an area to unite and operate one plant cooperatively. Also, producers shipping milk to a dealer wishing to sell his plant have often formed a cooperative to acquire and operate the plant, thus increasing their market security and earnings.

Some bargaining associations have entered fluid milk distribution to preserve a market for members where a customer dealer wished to sell his plant. In other cases, some cooperatives with milk manufacturing facilities have naturally expanded into fluid milk distribution.

Many of the fluid milk distributing cooperatives were formed during two 5-year periods of marked activity, 1919-23 and 1932-36. Unfavorable economic conditions were the principal reasons for the rapid growth during these years. During the first period, milk prices lagged behind prices for other agricultural products, but a shift to other lines of production was not attractive to fluid-milk producers located near a city market. In the second period, a wide gap developed between farm and retail prices for milk.

Records over the years are scanty on the number of cooperatives that primarily bottled and distributed fluid milk. Five were active in 1915. By 1940, there were about 100. Another 75 distributed some fluid milk as a sideline activity. In 1973, some 85 cooperatives distributed fluid milk, 40 as their major activity. By 1980, 59 cooperatives were packaging fluid milk; their share of fluid processing in the Nation has significantly increased.

Operations of Dairy Cooperatives

To effectively represent members and to operate efficiently in the business community, a cooperative must be recognized as a legal entity. In most cases dairy cooperatives have established legal status as an incorporated business. Many of the early dairy cooperatives were organized under the States' general corporation statutes. With the passage of special "agricultural cooperative" or "cooperative marketing" statutes by every State, cooperatives no longer use the general corporation statutes.

A cooperative's organizational documents, articles of incorporation and bylaws, describe its basic structure and internal operations. Generally, they include rules concerning: (1) membership qualification and suspension or terminations; (2) meetings of members, including voting rights; (3) the qualification, election, and duties of directors and officers; (4) duties of the manager; (5) use of committees; (6) capital structure; (7) rules of cooperative operations, including distribution of net margins; (8) use of capital retains and revolving capital; (9) dissolution and property interest of members; (10) end of fiscal year; (11) amendment provisions; and (12) other items necessary or desirable under the relevant State statute.

Organizational structure has varied between dairy cooperatives because of the economic circumstances of producers and their ideas for dealing with milk marketing problems. State and Federal law has also influenced cooperative structure and operations. For example, cooperatives must meet certain legal provisions to qualify for certain exemptions from antitrust laws, and others under the Federal Internal Revenue Act, to borrow from the bank for cooperatives, and to qualify as a cooperative in Federal milk marketing orders.

Operations of dairy cooperatives are greatly influenced by the uniqueness of milk. It is highly perishable and must be refrigerated immediately and processed within 2 or 3 days. It is bulky, causing transportation to make up a large part of the farmer's milk marketing costs. It

is assembled in small lots requiring the combined shipments from several farmers for low cost farm-to-plant hauling.

Dairy farmers do not enjoy the freedom of being able to store their milk on the farm for weeks while they individually seek a market. Neither can dairy farmers easily switch to another farming enterprise. Consequently, their search for market security and reasonable milk prices has led to relatively heavy reliance on cooperative marketing.

While each dairy cooperative has been organized and operated in a manner that responds to farmers' marketing problems, they can generally be categorized into four basic types: manufacturing, federated sales, raw milk sales, and bottling.

Manufacturing Cooperatives

Dairy cooperatives that primarily used members' milk and cream in manufacturing dairy products were the first to organize, and prior to the 1970's were the most numerous. Initially, they operated small creameries and cheese plants. The small creameries have either disappeared or shifted to other operations. Although the number of small cooperatives making cheese has greatly declined, some continue.

Over the years, manufacturing cooperatives have had to change to survive. Early cooperatives established producer pay prices largely on a net pool basis: gross returns less expenses and deductions for capital purposes. With increases in the number of cooperative and noncooperative milk manufacturing plants, the payment system became one of competitive prices limited at times by the cooperative's ability to pay.

The trend toward large-scale plants to obtain reduced operating costs was evident by the 1920's. Milk condensing and drying facilities made the nonfat portion of milk marketable and encouraged the shift from farm-separated cream to whole milk. The increased demand for nonfat dry milk and Government assistance in building milk drying plants during the early 1940's accelerated the shift from farm-separated cream to whole milk receipts. Even though small creameries may have added facilities for receiving whole milk and shipping the skim milk, they continued to face the long-term problem of maintaining a pay price competitive with the butter-powder and other whole milk manufacturing plants. Some small creameries have become milk receiving and shipping organizations.

Grade A milk producers began using farm bulk tanks in the 1950's. By the 1960's, producers of manufacturing grade milk were installing

farm bulk tanks. Increased supply mobility of tank-assembled milk widened fluid milk market supply areas. Milk delivery requirements for qualifying producers to participate in Federal milk order pricing pools have permitted manufacturing cooperatives to participate in fluid milk markets. Thus, producers of non-grade A milk installing farm bulk tanks were often encouraged to change their production to qualify for grade A milk production and become shippers to fluid milk markets.

In their efforts to maintain attractive producer prices, manufacturing cooperatives have continually worked to reduce costs, improve operating efficiency and the quality of their milk supply and products, use milk to produce high return products, and develop a secure, reasonably priced market for members. Most manufacturing cooperatives have become associated with fluid milk markets as an outlet for milk from members shipping grade A milk. Many small manufacturing cooperatives have merged with a large cooperative. The resulting multiplant cooperatives have given large-scale plants the flexibility needed to handle reserve fluid milk supplies and to manufacture products with greater market demand.

Dairy cooperatives have gained some market stability from the Government's dairy price support program. The Commodity Credit Corporation (CCC) stands ready to buy any quantity of butter, powder, and cheese of acceptable quality at prices that would permit an efficiently operated cooperative plant to pay the support price for milk used in manufacturing. This has partially helped many manufacturing cooperatives concentrate on building efficient plant operations.

Competition for milk supplies has often pushed producer prices above the price support level in the heavy non-grade A milk-producing areas of Minnesota and Wisconsin. These higher prices are used in establishing the minimum price for grade A milk used in manufacturing (Class III) in Federal milk marketing orders. They are also used as a price mover in establishing Class I prices.

Members of manufacturing cooperatives enjoy the advantages of a relatively secure market for their milk and the opportunity to participate in margins from these operations. Most of the larger manufacturing cooperatives emphasize new or expanded processing programs directed toward commercial market demand. These include both consumer and institutional packaging of butter and cheese in various packages and forms under their own and private labels and development of specialized food products such as de-lactosed whey and dried cheese blends. With additional processing, manufacturing cooperatives are working to capture a larger share of the farm-to-consumer margins.



Major dairy cooperatives, such as Land O'Lakes, Inc., Associated Milk Producers, Inc., and Dairymen, Inc., offer a wide variety of dairy products in their own consumer-brand packaging.





Federated Sales Cooperatives

Small milk manufacturing cooperatives soon recognized they had little or no voice at the marketplace. They recognized the need to join with neighboring cooperatives in developing a grading and packaging system to assure markets by providing city buyers a continuing supply of consistently high-quality products.

Early product sales cooperatives were federated organizations that generally operated central packaging and distributing plants. Initially, they marketed mostly butter and cheese, adding other products as member cooperatives expanded and diversified. Considerable field service work was done with member cooperatives to obtain delivery of high-quality products.

With the trend toward larger plants, several of the product sales cooperatives integrated into milk manufacturing and processing. Some disappeared during the 1960's through mergers or consolidations that resulted in large regional bargaining-operating cooperatives. Those few continuing into the 1980's have become primarily the sales agents for a group of manufacturing and bargaining-operating cooperatives.

Raw Milk Sales Cooperatives

Raw milk sales cooperatives primarily market raw whole milk to plants and dealers. While they generally began as "bargaining associations" with a membership that shipped milk to one or more handlers in a city fluid milk market, some have expanded their marketing to include not only delivery of milk supplies tailored to their handlers' needs but also the manufacture of the reserve milk supply in the cooperatives' own plants. Thus, raw milk sales cooperatives can be divided into two categories, "limited service" or pure bargaining and "bargaining-operating."

Limited Service Cooperatives

Unable to bargain successfully with fluid milk handlers, early limited service cooperatives often resorted to milk strikes or withheld supplies to obtain higher prices. At best, resulting gains proved to be only short term. Efforts to improve milk marketing conditions through Government assistance led to the development of State and Federal milk marketing orders. Among other things, these orders require handlers to pay minimum prices based on the use made of the milk. They also provide

for pooling handler payments for all use classes and computation of the order uniform blend prices to producers. In regulated markets, limited service cooperatives monitor market conditions and work to improve order provisions.

Federal milk marketing orders require cooperatives to perform certain marketing services if their members are to be exempted from a marketing service deduction, which generally ranges from 3 cents to 7 cents a hundredweight. The amount is determined by the market administrators' costs for providing specified services to nonmember producers. Limited service cooperatives have often financed their marketing service programs through deductions about equal to the order's deductions.

The larger cooperatives generally employ a general manager and a staff that includes laboratory technicians to check on test weight and quality of milk, field representatives to build membership and encourage milk quality, and personnel to prepare and distribute market information and represent the association in Federal and State milk order hearings.

Typically, producers are responsible for farm-to-plant milk hauling, even though deliveries by members of limited service cooperatives are often made at the direction of the handler. The handlers generally arrange for manufacturing plants to handle milk not needed by their fluid milk plants.

In Federal order markets, the minimum Class I prices for milk are lowest in those markets near the heavy milk supply area in Minnesota-Wisconsin. In most other markets the order Class I prices increase with distance from the Minnesota-Wisconsin area, but at a rate less than milk hauling costs from this area to the markets. Thus, handlers having to obtain some of their milk from the Minnesota-Wisconsin area could experience higher milk costs than competing handlers who obtain a full supply at the local market's order price. Because handlers are primarily concerned that milk is of good quality and competitively priced, limited service cooperatives have at times been able to obtain price increases that help to equalize the price for local milk with the cost for out-of-market milk. In some markets, handlers have even supported over-order prices to develop additional local milk supplies.

With increased mobility of tank-assembled milk and greater specialization in distribution by handlers, limited service cooperatives are finding their impact in the market is diminishing. Some survive by affiliating with more integrated cooperative associations while others form a federated organization with other small associations to provide needed services. Some have close working relations with the handler receiving their milk. Because this is their only feasible market outlet, they are often viewed as captive cooperatives. Where handler-customers believe the

benefits received outweigh service costs incurred to maintain the cooperatives, they will likely continue.

A large number of cooperatives that formerly operated small creameries and cheese plants now ship their entire milk supply to other plants. Some operate milk receiving stations while others deliver their milk directly to a selected milk manufacturing plant. Even though their milk generally goes to large cooperative plants, they could be viewed as limited service raw milk sales cooperatives. However, with full conversion to farm bulk tanks and increased movement of milk directly from farms to manufacturing plants, the need for these cooperatives is declining. Although viewed presently as raw milk sales cooperatives, they are merely a passing stage in the restructuring of manufacturing cooperatives.

Bargaining-Operating Cooperatives

More integrated raw milk sales cooperatives operate reserve milk manufacturing plants and generally provide handler-buyers with milk supplies tailored to their plant needs. They also offer a fuller array of services such as directing the farm-to-plant movement of milk, collecting from buyers for milk and other products sold, making payments to producers, and providing other needed services to producers and handlers.

The restructuring of raw milk sales cooperatives into large centralized cooperatives serving multimarket areas during the late 1960's and early 1970's improved overall marketing efficiency. For example, these centralized cooperatives have taken steps to better organize milk assembly routes and move milk to plants on a least-cost basis, locate and operate manufacturing plants to best handle the area's reserve milk supply, integrate marketing of manufacturing and reserve grade A milk, develop a centralized field service program, and centralize producer payroll and bookkeeping activities.

Disposition of reserve grade A milk has become increasingly a marketing burden in markets with relatively high Class I use. Wide daily and monthly fluctuations in volume result in a relatively low utilization of manufacturing plant capacity and a high unit operating cost, particularly during the market's peak-day Class I needs.

While eastern and southern markets have often provided higher prices for manufactured dairy products than midwestern markets, the price benefits often are not large enough to offset the higher reserve milk manufacturing plant costs. Losses suffered by larger bargaining-operating cooperatives in handling this reserve grade A milk are often recouped through over-order prices or by marketing service charges on sales of milk for fluid use.

Some noncooperative fluid milk processing firms worsen the reserve milk handling problem by purchasing part of their supply from independent producers and limited service cooperatives. They may rely on the regional bargaining-operating cooperatives to balance their fluctuating supply needs. These buying practices increase the reserve manufacturing plant's per unit costs borne by members of bargaining-operating cooperatives and enable unaffiliated producers to avoid all or at least part of such costs.

Regulatory agencies establish minimum class prices to be paid by a handler of first receipt. Service charges added to the minimum Class I prices by bargaining-operating cooperatives are not part of the regulatory system, and can be undermined by independent producers and competing limited service cooperatives that manage to avoid marketing service costs. As counter measures, bargaining-operating cooperatives often attempt to sell customer-handlers either their full supply requirements or an agreed portion of their Class I supply needs.

Some cooperative leaders question the ability of bargaining-operating cooperatives to maintain a strong market position with a marketing program that excludes packaging and distributing fluid milk, particularly, questioning whether milk marketing regulations should be terminated. The cooperatives have a stake in maintaining fluid milk outlets for members' milk. Also, they are concerned that market outlets for packaged milk be adequately served and that processor costs and margins not be so excessive as to substantially reduce sales volumes.

Several large regional bargaining-operating cooperatives have begun fluid milk processing or are actively studying opportunities for entering this field, particularly where customer milk buyers wish to sell their plants. This move largely accounts for the increase in cooperatives' share of the Nation's fluid milk processing from 9 percent in 1964 to more than 16 percent in 1982.

Bottling Cooperatives

Cooperatives that primarily bottle milk were usually started by producers who believed a bottling cooperative could return a higher net price than other dealers, either through a raw milk sales cooperative or by individual sales. Many of these bottling cooperatives began by purchasing a plant and business from another dealer. Others combined the operations of producer distributors into a new plant. In some cases, cooperative creameries and raw milk sales cooperatives added milk bottling to their operations.

Because fluid milk and related products are highly perishable, plant operations must be geared to product sales rather than milk production. Thus, bottling cooperatives face supply-balancing problems in maintaining milk supplies about equal to plant needs. They differ from other firms in that membership includes marketing obligations prohibiting cooperatives from reducing surplus milk by not accepting milk from selected producers.

In some of the early bottling cooperatives, members delivered only the amount of milk the cooperative needed and disposed of their share of the reserve milk individually. This generally required low-volume, high-cost manufacturing facilities or arrangements with manufacturing plants for handling the unneeded milk supplies.

Bottling cooperatives historically accepted new members only when they needed milk and then, only those producers required to provide the additional supply. They usually tried to balance milk receipts with Class I use. They generally opposed using marketwide pooling arrangement because it spread the low price returns for reserve milk among all producers.

With fluid milk markets becoming largely regulated by State and Federal milk marketing orders with marketwide pooling provisions, some bottling cooperatives now find it advantageous to minimize their supply-balancing problem by permitting member milk volume to decline below supply needs and then to obtain additional milk supplies from other cooperatives.

Bottling cooperatives have generally followed one of the following policies in determining producer milk prices. A few calculate an actual monthly pool price, based on sales returns and expenses, and pay patrons this price less deductions for capital purposes agreed upon in advance. A number pay patrons on a competitive monthly price basis even though this may result in profits or losses for the operation. Others establish a pay price periodically that continues until they determine a new price based on operations and market conditions.

The 1950's brought a number of technological changes to the fluid milk industry that required substantial increases in capital investments and volume of milk processed. With fluid milk sales relatively constant, many bottling plants were unable to compete and disappeared, many through merger or acquisition by other dairy cooperatives.

Integration of the food chains into fluid milk bottling and the disappearance of home delivery milk have greatly reduced sales for fluid milk bottling cooperatives, particularly in the larger cities. A few have survived with sales largely through their own convenience stores. Others distribute milk through the smaller food chains and independent stores,



A major delivery change in the decades of the 1950s and 1960s was the disappearance of home delivery when supermarket chains were able to offer milk at lower prices. The Flav-O-Rich products on the supermarket shelf below are brands, Dairymen, Inc., Louisville, KY.



packaging their product under a number of private labels in addition to the cooperative's brand.

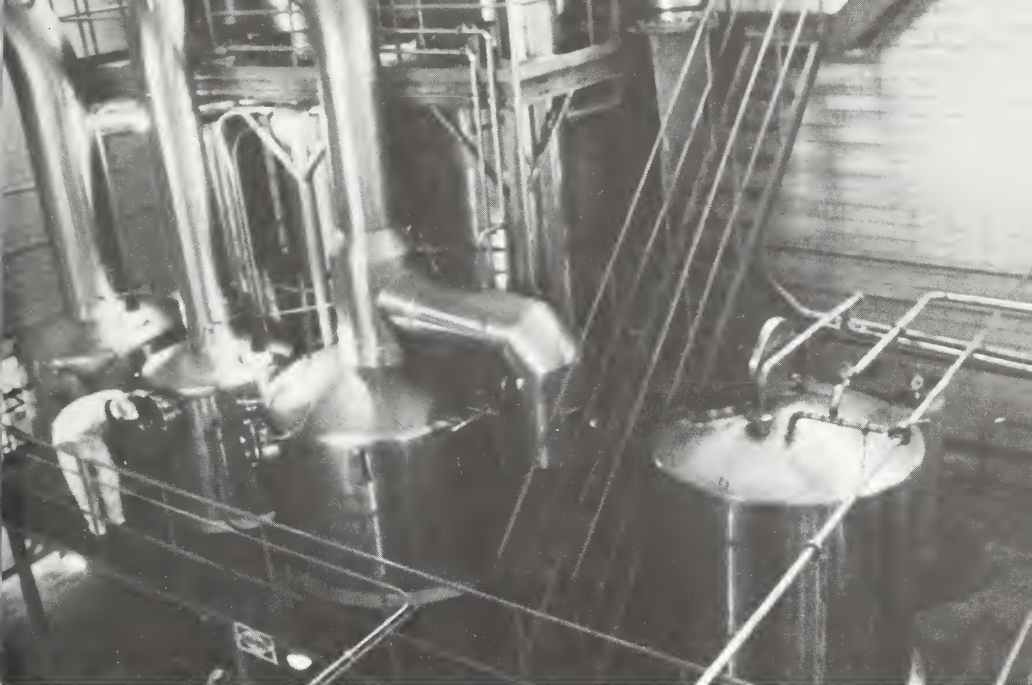
Nearly all bottling cooperatives were organized before the 1960's. Most bottling cooperatives have been able to accumulate the relatively large equity investment per member required in bottling through retained earnings, capital retains, asset appreciation, or some combination. With the continuing rise in capital requirements and the risks in a very competitive industry, some bottling cooperatives have merged with larger cooperatives. It is possible that in the future other fluid milk bottling cooperatives will also choose this method of spreading member risk and the equity capital financing burden over a larger and more stable membership base.

Financing Dairy Cooperatives

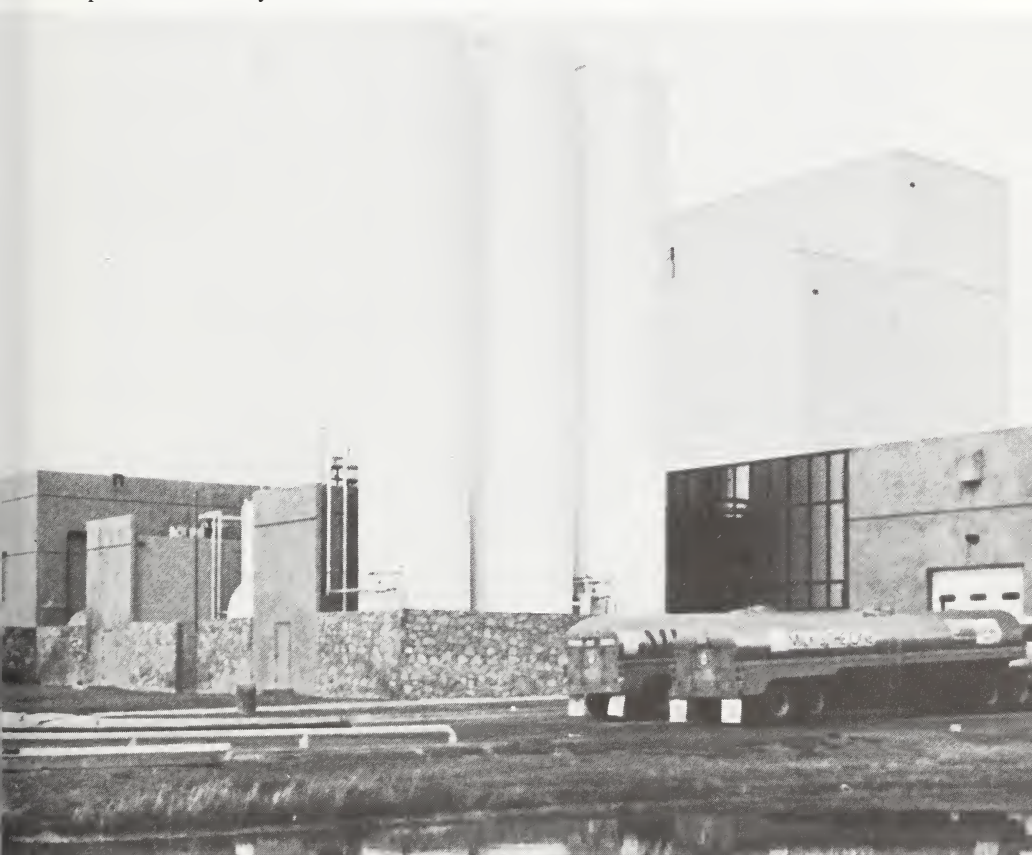
Cooperatives differ from other types of business in that the users are also the owners who establish operating policies and must provide most of the operating capital. This equity capital includes those funds that the cooperatives obtained for capital purposes without assuming a legal obligation to redeem at a stated time. Debt capital, on the other hand, is obtained largely from nonowners and the cooperative incurs legal liability to return it as agreed.

Many of the early cooperatives, particularly those with plant facilities, were organized with capital stock. Each member purchased a share of common stock that gave voting privileges. Preferred stock with a dividend rate reflecting reasonable returns for capital (not to exceed 8 percent) was sold largely to members. Many of the cooperatives organized without capital stock began as bargaining associations (raw milk sales cooperatives). Their initial equity capital came from the sales of membership certificates or membership fees.

Once started, dairy cooperatives have relied mostly on margins from operations for equity capital. Through efficient plant operations they generally are able to pay producers a competitive price for their milk and earn a reasonable margin for operations. Raw milk sales cooperatives generally establish marketing service fees that provide income greater than costs, leaving a small operating margin. Retention of margins has become the preferred method of capitalizing cooperatives. By revolving or paying back the oldest retained margins first, the capital burden is borne by producers in accordance with their use of the organization. Members must include the retained margins allocated or distributed to them in their taxable incomes. Beginning in 1962, cooperatives' tax



Dairy farmers are challenged to find the capital to build expensive processing facilities, such as these evaporators used in producing nonfat dry milk in this Mid-America Dairymen, Inc., plant and this milk-balancing plant owned by Associated Milk Producers, San Antonio, TX.



treatment required that on qualified patronage refunds at least 20 percent had to be distributed in cash.

The technological developments that began in the 1950's greatly accelerated the capital needs of dairy cooperatives. With new restrictions on qualified patronage refunds, cooperatives began to deduct per-unit capital retains from members' milk payments to obtain capital.

In 1976, dairy cooperatives had \$583 million in equity capital. They had acquired 68 percent of this from retained margins, 26 percent from per-unit capital retains, and 6 percent from the sale of stock and other equity paper to members. Ninety percent of the total equity capital was evidenced by certificates of allocated credits, 9 percent by capital stock (sales and distribution), and 1 percent by unallocated reserves and membership certificates.

Dairy cooperatives, particularly bottling and manufacturing cooperatives, were depending heavily on debt capital. While only 206 dairy cooperatives had borrowed money in 1976, the amount borrowed totaled \$513 million. More than three-fourths was borrowed from banks—65 percent from the banks for cooperatives, and 11 percent from commercial banks. Some 20 percent came primarily from members by issuance of debt securities, and 4 percent came from other sources.

In 1976, dairy cooperatives had about \$2.0 billion in total assets of which \$1.3 billion were current assets and \$536 million fixed assets. Equity capital was slightly larger than the fixed assets and represented 29 percent of total assets. Debt capital represented 26 percent of total assets, while 45 percent were represented by various other types of liabilities including amounts due for members' milk and other accounts payable.

Trends toward much larger capital needs to finance the growth of dairy cooperatives have serious implications for both creditors and farmer-members. The cooperative principle "service at cost" precludes the possibility of profit participation often demanded by creditors who supply a business with a large share of its total capital requirements. Creditors limit their risks by insisting members supply most of the capital and by keeping the amount loaned below the point where debt service cost might reduce the cooperative's ability to survive. Thus, much of the capital needed by dairy cooperatives must come from members.

To best meet their capital needs, a number of dairy cooperatives are using new capital plans and operating arrangements. For example, some dairy cooperatives have shifted from the capital revolving plan to a base capital plan in which each member invests a fixed amount based on past milk production. The member's capital base does not change from year to year unless the cooperative's total capital requirements or the member's milk production changes significantly.

Dairy cooperatives are beginning to join with other cooperatives and in a few instances with noncooperative food processing and marketing firms to provide members marketing services. In other cases, facilities may be obtained through lease arrangements.

By 1990, dairy cooperatives will still be financed primarily by revolving funds obtained by retained margins and per-unit capital retains. Members must supply increased capital if dairy cooperatives are to fulfill income and market security objectives.

National Organizations

Dairy cooperatives and their members belong to several specialized national organizations concerned with legislation, advertising, sales promotion, merchandising, marketing, public relations, product research, and obtaining dairy supplies.

National Milk Producers Federation

The National Milk Producers Federation (NMPF) was founded in Chicago in December 1916 and is the oldest of the national cooperative organizations.

NMPF's membership is composed solely of milk marketing cooperatives and their federations from across the Nation. Because milk is the only commodity produced in virtually every State, the consensus of the NMPF's membership is extremely important to agricultural legislation.

NMPF's work is directed primarily toward legislative efforts in five major areas—price supports, milk marketing orders, the cooperative structure, dairy product import, and product integrity. NMPF monitors other areas that affect these, including energy, transportation, nutrition, antibiotics, pesticides, environmental issues, animal disease control, and consumer attitudes and trends. NMPF also works within its membership, other industry groups, and the Government to mold policies favoring dairy farmers, cooperatives, and consumers, as economic conditions, technology, and consumers' interests change.

NMPF is governed by a board of directors and an executive committee selected from the board. Member cooperatives fund NMPF directly and establish its policies. The policies are the only national statement of dairy policy developed exclusively by dairy farmers through their cooperatives.

Once these policies are established, NMPF provides a mechanism to further them legislatively and administratively at the national level. NMPF serves as a liaison between Congress, Government agencies, and member cooperatives.

NMPF's office is located at 1840 Wilson Blvd., Arlington, VA 22201.

United Dairy Industry Association

In 1970, the United Dairy Industry Association (UDIA) was formed by the American Dairy Association (ADA), the National Dairy Council (NDC), and Dairy Research, Inc. (DRINC) to increase the sales of U.S. milk and dairy products.

Although dairy cooperatives, in most cases, are not direct members of this association, more than 96 percent of the dairy farmers in the United States support UDIA, many through a setaside program administered by their cooperative. A house of delegates governs the organization. These delegates are apportioned according to each organization's investment in UDIA's total promotion program. In 1984, more than 147 delegates representing dairy producers, processors/handlers, and dairy council organizations from outside UDIA served as the governing body.

The total unified budget of UDIA and its investing members served will likely exceed \$90 million in 1985. Of this, about 80 percent will be retained at the regional and local levels for UDIA's promotional programs, which benefit the entire dairy industry. The combined operating budget for UDIA's national programs in 1984 totaled about \$9.5 million.

Two of UDIA's major corporate objectives are:

1. Develop and coordinate a total promotion program for national, regional, and locals levels, that will:

- a. increase sales and per capita consumption of milk and milk products,

- b. optimize return on investment of UDIA investing members, and

- c. contribute materially to the health and well-being of the American public.

2. Coordinate the funding, administration, and programs of its operating divisions as follows:

- a. research - market and economic, nutrition, nutrition education, and process, and product development.

- b. education - nutrition, sales training, in-service.

- c. advertising - consumer and professional.

- d. sales promotion - point of purchase, cooperating campaigns.

e. communications - dairy industry, consumer, Government, scientific, educational, and health professionals.

The ADA operating arm of UDIA was originally organized in 1940 by a group of dairymen and handlers. Dairy farmers now fund ADA through the UDIA umbrella organization. ADA uses local and national consumer advertising through print, radio, and TV media and in-store promotion to promote and advertise dairy products on a nonbrand basis. Dairy department and supermarket managers are also advised how to handle and sell dairy products.

National Dairy Council. NDC was organized more than 70 years ago to combat a serious spread of hoof-and-mouth disease among cattle in several States. It has evolved into conducting nutrition research and education that help "promote optimum health and human welfare through adequate use of milk and its products" NDC's nutrition research and education are funded by UDIA.

Dairy Research, Inc. The DRINC part of UDIA does dairy product and process research and development. It works with noncooperative as well as cooperative firms, universities, and others in expanding outlets for dairy products and developing processes that will improve the product and its manufacture.

The national headquarters for UDIA is in the Dairy Center at 6300 North River Road, Rosemont, IL 60018.

Milk Industry Foundation/International Association of Ice Cream Manufacturers

Some dairy cooperatives that operate dairy processing facilities belong to the Milk Industry Foundation or the International Association of Ice Cream Manufacturers, or both; two separate organizations managed by the same staff.

The Milk Industry Foundation (MIF) is a trade association representing slightly fewer than 400 processors and distributors of fluid milk and its products. Member companies operate more than 800 plants and process about 75 percent of the total fluid milk processed, bottled, and consumed in the United States. In addition to fluid milk, MIF represents its members' interests in a wide range of associated products—yogurt, cottage cheese, dips and dressings, other cultured dairy products, eggnog, and similar fluid milk products. MIF also represents its members on regulatory and legislative matters.

The International Association of Ice Cream Manufacturers (IAICM) is composed of slightly fewer than 300 member companies

operating about 650 plants that manufacture about 80 percent of the total ice cream and related products consumed in the United States. The products include all their various forms, such as prepackaged, bulk for hand dipping, novelties, quiescently frozen novelties, water ices, and so forth.

Both associations jointly own and operate the Dairy Training and Merchandising Institute. This organization conducts marketing research and operates numerous schools, symposia, and seminars to train industry personnel in various milk and ice cream operations. Among the courses offered are executive management, sales, marketing management, distribution management, financial management, dairy technology, and others.

MIF and IAICM have an office at 910 17th Street, NW, Washington, DC 20006.

Other Trade Associations

Dairy cooperatives, especially those operating processing or manufacturing plants, may belong to several national associations in addition to those discussed above. These include the American Dry Milk Institute, American Butter Institute, and the National Cheese Institute. Many of the larger dairy cooperatives belong to the National Council of Farmer Cooperatives.

One provision of the Dairy and Tobacco Adjustment Act of 1983, strongly supported by dairy cooperatives, created a National Dairy Promotion and Research Board. Its 36 members are dairy farmers, most of whom were nominated by dairy cooperatives. The Board oversees the collection and disbursement of a congressionally mandated 15 cents per hundredweight checkoff to promote the consumption of fluid milk and dairy products. The Board is coordinating its large-scale promotion programs with other dairy promotion programs such as those operated by UDIA and the Milk Industry Foundation.

Challenges for the Future

Dairy cooperatives will continue to perform a vital role marketing their members' milk. In fact, several trends observed in recent decades suggest an even more important need for cooperatives in the dairy industry. How well dairy cooperatives respond to these trends, and how well they serve their member-owners, will depend on the attitudes and responsiveness of members and their elected directors and the skills of hired management. Following are some of the more important trends and challenges:

1. Surviving dairy farms will have larger herds and be more heavily capitalized. Dairy cooperatives will need to provide a high quality and



Dairy cooperatives' activities range from farm research, such as Land O'Lakes' "Answer Farm," to joint consumer information and promotion programs nationwide.



responsive package of services to these farmers such that the cooperatives can successfully and justifiably compete for essential owner equity capital with on farm capital needs.

2. Because noncooperative buying handlers or dealers of milk will continue to decline in number but become much larger, cooperatives must grow in size and scope to provide a milk supply tailored to these buyers' needs. The many small pure bargaining cooperatives that compete with larger regional bargaining-operating and manufacturing cooperatives will find it more difficult to obtain secure milk markets. Most of these organizations will have to reevaluate their objectives with respect to whether or not they provide a needed service to members.

3. More of the Nation's milk supply, both on an absolute and percentage basis, will be used in manufacturing, rather than fluid processing. Dairy cooperatives need to make large new capital investments in efficient, competitive milk manufacturing facilities, requiring new and higher levels of farmer equity investments.

4. Rapid expansion of chain food retailers into vertically integrated fluid milk processing will continue to drive traditional full service fluid milk processors out of business. In some markets, dairy cooperatives will need to acquire or build fluid processing plants to obtain market security and to effectively service the nonintegrated segment of the fluid market. New member equity capital investments will be required to effectively compete in the capital intensive, fluid milk processing business. Cooperatives must consolidate further to spread risk and capital needs through larger membership bases.

5. Expected changes in the political philosophy and policies guiding the milk price support program and both Federal and State fluid milk marketing orders will affect cooperatives. Cooperatives will become far more involved in merchandising completely finished consumer packaged products to the end users or retailers. Price support purchases of bulk commodities such as barrels of cheese or bags of powder will likely be used only as emergency underpinning of short-term low prices, rather than as a basic market outlet. In like manner, milk orders will serve less as a price-making vehicle and more as an audit function and a means of establishing reasonably orderly marketing. In this setting, milk producers, if they wish to receive an equitable return from the market for dairy products, must involve their cooperatives much more deeply in all phases of processing, manufacturing, packaging, and merchandising dairy products.

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**U.S. Department of Agriculture
Agricultural Cooperative Service
Washington, D.C. 20250**

Agricultural Cooperative Service (ACS) provides research, management, and educational assistance to cooperatives to strengthen the economic position of farmers and other rural residents. It works directly with cooperative leaders and Federal and State agencies to improve organization, leadership, and operation of cooperatives and to give guidance to further development.

The agency (1) helps farmers and other rural residents develop cooperatives to obtain supplies and services at lower cost and to get better prices for products they sell; (2) advises rural residents on developing existing resources through cooperative action to enhance rural living; (3) helps cooperatives improve services and operating efficiency; (4) informs members, directors, employees, and the public on how cooperatives work and benefit their members and their communities; and (5) encourages international cooperative programs.

ACS publishes research and educational materials and issues Farmer Cooperatives magazine. All programs and activities are conducted on a nondiscriminatory basis, without regard to race, creed, color, sex, age, handicap, or national origin.